Supreme Court, U.S.
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No. 98-1604

IN THE

Supreme Court of the United States

WALTER YOUNAS STEWART,

Petitioner,

v.

DENNIS JOSLIN, Certified Public Account,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

RESPONDENT'S BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether a Chapter 12 plan can void cross-collateralization clauses contained in separate mortgages to the same creditor where the plan does not address such clauses.

STATEMENT OF THE CASE

This case involves four Deeds of Trust cross-collateralizing each of four Notes owned by Respondent Dennis Joslin ("Joslin"). Petitioner, Walter Stewart ("Stewart") defaulted on the four Notes and filed for protection under Chapter 12 of the Bankruptcy Code. Under his Chapter 12 Plan, Stewart valued the underlying collateral and committed to repay a total of $92,231.35 out of the $256,000.00 he originally borrowed under the four Notes. The Original Confirmation Order provided that:

> All Deed of Trust lien holders shall be allowed to maintain their respective liens on the property described in the Schedules and the Chapter 12 Plan, to the full extent of the Plan Secured Values.

Stewart then moved to modify his plan by extending the pay-out on the four Notes over a period of 15 years (the "Modification Order"). Stewart defaulted again by failing to make the extended payments under the modified Chapter 12 Plan. Joslin then sued for judicial foreclosure under the four Deeds of Trust. Stewart moved for summary judgment in the District Court claiming his Chapter 12 Plan and/or the subsequent Modification Order implicitly voided the cross-collateralization clauses in the four Deeds of Trust. Joslin also moved for summary judgment.

None of Stewart's prior bankruptcy pleadings, orders or motions addressed the subject of cross-collateralization. As such, the District Court denied Stewart's Motion for Summary Judgment and granted Joslin's Motion for Summary Judgment, finding, among other things, that the cross-collateralization clauses in the four Deeds of Trust had not been affected by the Stewart bankruptcy. The Court of Appeals agreed, holding that

"the issue of the cross-collateralization clauses was not the subject of any of the bankruptcy proceedings."

REASONS FOR DENYING THE WRIT

The Fifth Circuit Opinion does not conflict with (i) the language of Bankruptcy Code § 1225(a)(5), (ii) the Eighth Circuit Opinion in *Harmon v. United States through Farmers Home Administration*, 101 F.3d 574 (8th Cir. 1996) or (iii) the Second Circuit Opinion in *In Re Kerwin* 996 F.2d 552 (2nd Cir. 1993). The lien rights retained by Joslin are completely consistent with applicable bankruptcy law, under the facts of this case.

I.

THE DECISION BELOW RECOGNIZES THAT A DEBTOR'S FORCED INVALIDATION OF A CREDITOR'S LIEN RIGHTS MUST BE ACCOMPLISHED THROUGH THE EXPRESS PROVISIONS OF A CHAPTER 12 PLAN.

Throughout this litigation, Stewart has repeatedly argued that the cross-collaterlization clauses contained in the Deeds of Trust were voided by Stewart's Chapter 12 Plan. Although Stewart argued that the cross-collaterlization issue was previously litigated in his Chapter 12 Bankruptcy, this assertion is simply not true. The cross-collateralization clauses were not even addressed in either (i) Stewart's Chapter 12 Plan or (ii) in the original confirmation order.

The Bankruptcy Code provides that a Chapter 12 plan *may* "modify the rights of holders of secured claims . . . or leave unaffected the rights of holders of any class of claims," 11 U.S.C. § 1222(b)(2). Although Stewart's Chapter 12 Plan

could have modified cross-collateralization rights under the four Deeds of Trust, the Plan did not do so. It left such rights "unaffected." Indeed, Stewart's Chapter 12 Plan provided that "Deed of Trust lienholders (sic) will be allowed to maintain their respective liens on the property. . . ."

Stewart also asserted that a Modification Order effectively stripped the cross-collateralization clauses.[1] However, the Modification Order did not discuss cross-collateralization clauses. Finally, Stewart argued that the Modification Order, taken with the provisions of 11 U.S.C. § 1222(b)(2) and 11 U.S.C. § 1225(a)(5)(B) acted to nullify the cross-collateralization clauses. The District Court and Court of Appeals each rejected this argument because any attempt to alter the cross-collateralization clauses in this fashion would have constituted an impermissible material modification of the Chapter 12 Plan.

II.

THE DECISION BELOW IS NOT INCONSISTENT WITH THE DECISIONS OF THE SECOND AND EIGHTH CIRCUITS WHEN CONSIDERING THE LIEN RIGHTS OF SECURED CREDITORS VIS-À-VIS THE RIGHTS OF DEBTORS UNDER CHAPTER 12 OF THE BANKRUPTCY CODE.

In his argument to this Court, Stewart argues that the Fifth Circuit's opinion in this case is in conflict with other opinions rendered by the Eighth and Second Circuits. However, no such conflict exists. The facts in the cases cited by Stewart are very

1. Interestingly, by arguing that the Modification Order terminated the cross-collateralization clauses, Stewart implicitly acknowledged that the Original Plan and Order Confirming Plan left the cross-collateralization clauses unaffected.

different than those in this case. Indeed, these other opinions do not even address the issue presented in this case. Stewart simply misinterprets *Harmon v. United States through Farmers Home Administration*, 101 F.3d 574 (8th Cir. 1996) and *In Re Kerwin* 996 F.2d 552 (2nd Cir. 1993).

In *Harmon v. United States through Farmers Home Administration*, 101 F.3d 574 (8th Cir. 1996) the Eighth Circuit dealt with an undersecured creditor who attempted to recover the *unsecured* portion of its claim. In *Harmon,* the creditor refused to acknowledge that its lien only encumbered the debtor's property up to the amount of its "allowed secured claim," as that phrase is used in 11 U.S.C. § 1225(a)(5)(B). Instead, the creditor demanded payment of its entire claim after the debtor's successful completion of a Plan, *i.e.*, both the secured *and* unsecured portion. In the present case, Joslin merely asserts that his cross-collateralization rights require Stewart to pay off all of his allowed *secured* claims (as that term is used in 11 U.S.C. § 1225(a)(5)(B)). Joslin has never demanded that Stewart pay off any portion of Joslin's substantial unsecured claim in order to obtain a release of the liens under the four Deeds of Trust. In addition, Stewart never completed his Plan. Stewart's attempt to pay off only one tract occurred after he defaulted on his obligations under his Plan.[2]

In *In Re Kerwin* 996 F.2d 552 (2nd Cir. 1993) the Second Circuit considered "whether a family farmer has a right in a Chapter 12 bankruptcy claim to satisfy fully an *oversecured*

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2. As noted in the Fifth Circuit Opinion below, "the other three parcels of land are essentially landlocked and cannot be reached except by the use of the first tract of land." Stewart's attempt to pay off only the first tract would have allowed Stewart to effectively deny Joslin access to the remaining property, after his foreclosure on the last three tracts.

creditor by transferring a portion of the creditor's collateral determined to be equal in value to the outstanding debt . . .". *In Re Kerwin*, 996 F.2d at 554 (emphasis added.) In the present case, Joslin's claim totaled $256,000.00, while his allowed secured claims totaled $92,231.35. Joslin was significantly undersecured.

In *In Re Kerwin*, the creditor attempted to retain a lien over that portion of the collateral retained by the debtor after the full satisfaction of the creditor's claim as part of a completed Chapter 12 Plan. Joslin is not attempting to assert lien rights in property that was retained by the debtor free and clear of liens under the terms of a completed Chapter 12 Plan. Joslin is merely asserting that certain cross-collateralization rights that were never addressed by Stewart's Chapter 12 Plan require Stewart to pay off the full amount of Joslin's "allowed secured claims" (as that phrase is used in 11 U.S.C. § 1225(a)(5)(B)) before obtaining a release of the liens created by the four Deeds of Trust.

CONCLUSION

The Bankruptcy Court had the power to invalidate the cross-collateralization provisions contained in the four Deeds of Trust under the express terms of (i) a confirmed Chapter 12 plan and/or (ii) an Order Confirming Plan. This was never done. The bankruptcy court's subsequent modification of Stewart's Plan could not have invalidated the cross-collateralization provisions without affecting an impermissible modification of the Chapter 12 plan.

Finally, the issues presented in this case were not addressed by either the *Harmon* court or the *In Re Kerwin* court. As such, the decision below is not in conflict with either of these other Court of Appeals opinions.

Respectfully submitted,

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